

Internal Revenue Service

Department of the Treasury
Washington, DC 20224

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Date:

February 19, 2009

Legend:

Fund A =

Fund B =

Fund C =

Trust =

Corporation =

Managing Company =

Type A Company =

Date 1 =

Date 2 =

State A =

State B =

State C =

Country =

Dear :

This is in response to your letter dated October 21, 2008 and subsequent correspondence dated December 30, 2008 and January 6, 2009, requesting a ruling that income earned from a Fund's investment in its wholly-owned subsidiary, which is a Controlled Foreign Corporation (CFC), constitutes qualifying income under section 851(b)(2) of the Internal Revenue Code of 1986, as amended (the Code).

Facts:

Fund A is a series of Trust, a State A business trust. Fund B is a State B corporation. Fund C is a series of Corporation, a State B corporation (collectively the Funds). The Funds are managed by Managing Company, headquartered in State C. Funds A and B have fiscal years ending on Date 1, and Fund C has a fiscal year ending on Date 2. All of the Funds are accrual method taxpayers.

Each Fund qualifies as a regulated investment company (RIC) under § 851 of the Code. Funds A and C are each a series of an open-end management investment company registered under the Investment Company Act of 1940, 15 U.S.C. 80a-1 et seq., as amended (the 1940 Act). Fund B is a closed-end management investment company registered under the 1940 Act.

Each Fund intends to form a wholly-owned, foreign subsidiary incorporated as a Type A Company under the laws of Country. Under the laws of Country, a Type A Company provides for limited liability for all holders of shares. A shareholder's liability is limited to the amount, if any, unpaid with respect to the shares acquired by the shareholder. Each subsidiary will file an election on Form 8832 to be taxed as a corporation pursuant to § 301.7701-3 of the Procedure and Administration Regulations.

The Funds represent that although each subsidiary will not be registered as an investment company under the 1940 Act, each subsidiary will comply with the requirements of section 18(f) of the 1940 Act, Investment Company Act Release No. 10666, and related SEC guidance pertaining to asset coverage with respect to transactions in commodity futures and other transactions in derivatives.

The Funds will invest a portion of their assets in their respective subsidiary, subject to the asset diversification limitations set forth in § 851(b)(3). Each subsidiary is expected to invest in commodities, commodity futures and notional principal contracts, but may also invest in securities or debt or hold cash.

Each subsidiary will be wholly owned by a Fund and, as such, the Funds represent that the subsidiaries will qualify as controlled foreign corporations (CFCs). Each Fund will include its respective subsidiary's "Subpart F" income for the taxable year in accordance with § 951.

Law and Analysis:

Section 851(b)(2) provides that a corporation shall not be considered a RIC for any taxable year unless it meets an income test (the Qualifying Income Requirement). Under this test, at least 90 percent of its gross income must be derived from certain enumerated sources. Section 851(b)(2) defines qualifying income, in relevant part, as –

dividends, interest, payments with respect to securities loans (as defined in section 512(a)(5)), and gains from the sale or other disposition of stock or securities (as defined in section 2(a)(36) of the 1940 Act) or foreign currencies, or other income (including but not limited to gains from options, futures or forward contracts) derived with respect to [the RIC's] business of investing in such stock, securities, or currencies

Section 2(a)(36) of the 1940 Act defines the term "security" as –

any note, stock, treasury stock, security future, bond, debenture, evidence of indebtedness, certificate of interest or participation in any profit-sharing agreement, collateral-trust certificate, preorganization certificate or subscription, transferable share, investment contract, voting-trust certificate, certificate of deposit for a security, fractional undivided interest in oil, gas, or other mineral rights, any put, call, straddle, option, or privilege on any security (including a certificate of deposit) or on any group or index of securities (including any interest therein or based on the value thereof), or any put, call, straddle, option, or privilege entered into on a national securities exchange relating to foreign currency, or, in general, any interest or instrument commonly known as a "security", or any certificate of interest or participation in, temporary or interim certificate for, receipt for, guarantee of, or warrant or right to subscribe to or purchase, any of the foregoing.

In addition, § 851(b) provides that, for purposes of § 851(b)(2), there shall be treated as dividends amounts included in gross income under §§ 951(a)(1)(A)(i) or 1293(a) for the taxable year to the extent that, under §§ 959(a)(1) or 1293(c) (as the case may be), there is a distribution out of the earnings and profits of the taxable year which are attributable to the amounts so included.

Section 957 defines a controlled foreign corporation (CFC) as any foreign corporation in which more than 50 percent of (1) the total combined voting power of all

classes of stock entitled to vote, or (2) the total value of the stock is owned by United States shareholders on any day during the corporation's taxable year. A United States shareholder is defined in § 951(b) as a United States person who owns 10 percent or more of the total voting power of a foreign corporation. Each Fund has represented that it will own 100 percent of the voting power of the stock of its respective subsidiary. The Funds are United States persons. Based upon the Funds' representations, each of the respective Subsidiaries will qualify as CFCs under these provisions.

Section 951(a)(1) provides that, if a foreign corporation is a CFC for an uninterrupted period of 30 days or more during any taxable year, every person who is a United States shareholder of this corporation and who owns stock in this corporation on the last day of the taxable year in which the corporation is a CFC shall include in gross income the sum of the shareholder's pro rata share of the CFC's subpart F income for the taxable year.

Section 952 defines subpart F income to include foreign base company income determined under § 954. Under § 954(a)(1), foreign base company income includes foreign personal holding company income determined under § 954(c). Section 954(c)(1)(A) defines foreign personal holding company income to include dividends, interest, royalties, rents, and annuities.

Subsidiaries' investments may generate foreign personal holding company income under § 954(c), which is subpart F income. Funds would therefore include in income their subsidiary's subpart F income for the taxable year in accordance with § 951.

Conclusion:

Based on the facts as represented, we rule that subpart F income of the subsidiaries that is attributable to the Funds is income derived with respect to the Funds' business of investing in the stock of subsidiaries, and thus constitutes qualifying income under § 851(b)(2).

This ruling is directed only to the taxpayers who requested it, and is limited to the facts as represented by the taxpayers. Section 6110(k)(3) provides that this letter may not be used or cited as precedent.

In accordance with the Power of Attorney on file with this office, a copy of this letter is being sent to your authorized representative.

Sincerely,

David B. Silber
David B. Silber
Chief, Branch 2
Office of Associate Chief Counsel
(Financial Institutions and Products)